Building Economic Diversity: Overcoming State Budget Revenue Shortfalls

Strategic Initiatives Position
Greater Albuquerque Chamber of Commerce Board of Directors
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<u>Situation</u>

The state budget is in difficult circumstances due to a significant loss of revenue from the decline in both the price and amount of oil and gas produced in the state. This decline precipitated the loss of 6,500 jobs and, consequentially, the loss of income and gross receipts tax revenues. Other jobs dependent on oil and gas production have likewise been adversely affected.

The estimated shortfall for the current budget year, FY17, is $458 million. The state concluded the last fiscal year, FY16, about $348 million short in revenues. The Governor plans to call the Legislature into special session at the end of September in order to address this issue.

State general fund revenues flowing directly from energy production comprise about 15% of the state general fund (in good years this figure is about 25%). This is about $1 billion of the approximate $6 billion general fund. In addition, this economic sector contributes substantially to gross receipts and income tax revenues. In the energy producing counties, for example, gross receipts taxes are down significantly: Eddy by 39.2%, Lea by 24.7% and San Juan by 4.9%, comparing FY15 to FY 16. Moreover, royalties and other taxes and fees support the state's two permanent funds, which, in turn, support education and capital improvement projects. Likewise, revenue has fallen to these funds.

For each $1 change in the price per barrel of oil, there is about a $10 million effect – either positive or negative- on the general fund. Oil prices in 2016 have bounced between a low of about $26/barrel to a high of about $50/barrel. For each 10-cent change in the price per thousand cubic feet of natural gas, there is approximately a $6.5 million effect on the general fund.

Since New Mexico oil requires more refining than "West Texas Intermediate Crude (WTI)", the benchmark for U.S. oil prices, New Mexico oil typically sells at about $5 per barrel less than WTI. The FY 2017 budget was built on the assumption of about $39 per barrel oil.

Recently, oil prices seem to be stabilizing and the rig count in New Mexico has increased somewhat. In fact, rigs are being added in the Permian Basin at a disproportionately faster rate than in most of the rest of the country. Therefore, there is some optimism that the worst has passed and drilling is set to resume again. However, it is still largely unknown how much time it will take for production to ramp up and for the state to once again see all of the different revenue benefits of this increased drilling activity.

Without question, the long-term solution to this problem is to increase economic diversity and grow the private sector in a way that decreases our over reliance on oil and gas production and federal government spending.

Over the last 48 months, 45 of those have seen growth in private sector employment with the greatest proportion outside the energy sector. Employment growth in recent months has been particularly strong and has more than overcome the loss of over 6,500 jobs in the energy sector in the past year. This illustrates that support for economic development by the Legislature and the Governor has taken root. We must stay the course – these recent changes have been noticed and New Mexico is now viewed favorably as a place to do business. By all accounts, our recruitment pipeline for new companies and business expansions is as full as it's ever been. We cannot afford to retreat from this hard won high ground.

Position

In order to achieve long-term economic diversity while managing the current revenue shortfalls, the Greater Albuquerque Chamber has adopted a strategic approach described in the following positions. We urge the Governor and the Legislature to incorporate this approach in their efforts to resolve the current budget dilemma.

Support:

- Retain funding for priority programs that are working to build economic diversity in New Mexico despite revenue shortfalls. Especially important are the Job Training Incentive Program (JTIP) and the Local Economic Development Program (LEDA).

  These two programs provide the resources needed to tip the scales of site selection in the state’s favor. Both programs are entirely performance based, i.e. results must be achieved and jobs created in New Mexico or there is no investment of state funds. These programs benefit both existing and new companies, rural and urban areas.

  Expanded funding of these programs recently enacted by the Legislature has increased the ability to respond to the large number of requests received for assistance. To cut funding in these critical areas would irreparably damage the state’s reputation as a reliable economic development partner and slam the brakes on future progress.

  In FY16, JTIP benefited sixty companies resulting in the training of 2,238 workers whose average wage is $18.04 per hour. The investment of $15.2 million of capital improvement projects under the LEDA program resulted in attracting $256.8 million in private capital investment for a 16.8 to 1 leverage ratio with the return expected to be even higher given the state's new $50 million plus commitment to the program. Both programs result in increased revenues for state and local governments.

- Retain vital “tax expenditures” (deductions, exemptions and credits) aimed at promoting investment, job creation and the overall competitiveness of our business climate. This would include past efforts to reduce pyramiding of gross receipts taxes, encourage investment in new start-up companies, create new jobs in the high-tech sector, and exempt locomotive fuel from taxation.

- Preserve reductions passed in 2013 to New Mexico's corporate income tax rate and the enactment of a single sales factor apportionment for manufacturers.

- Eliminate or modify other tax expenditures where it is conclusively determined that these incentives are no longer needed or needed in their current form.

Oppose

- Reject any new tax increases. Just as taking away well-conceived incentives would be counterproductive to growing the state's economy and, therefore, state government revenues, so would increasing taxes. Increased taxes dampen economic expansion. As New Mexico builds momentum towards growing jobs and business development, tax increases must be avoided as these would be counterproductive to economic recovery.

  A strategic approach to shaving state spending and reforming tax expenditures along with continuing economic development investment is the best path to growing revenues to meet the state's need. Tax increases are a short-term solution but with long-term adverse consequences.

- Exempting any segment of state government from critical examination. Public and higher education account for 60 percent of general fund expenditures and health care 25%. Only 15% of the state general fund goes for all other purposes, including economic development. To close the budget gap, all areas can and should contribute to the solution. To arbitrarily exclude any segment limits flexibility and biases any solution towards tax increases. Instead, clear-headed analysis should lead to elimination of inefficiency and ineffectiveness in favor of programs with proven records of success.